



## **Saving for School**

### RESPs are gaining in popularity

BY JOHN SCHOFIELD

Little Kathryn Ash has just about got her future figured out. The energetic eight-year-old from St. John's, Nfld., wants to be a teacher when she grows up although she sometimes changes her mind when she is angry with her father Don, a high-school vice-principal. Her 12-year-old sister, Jessica, thinks her mission in life is to be a veterinarian. For Ash and his wife, Frances, 37, a Revenue Canada assessor, what matters most is whether the girls can afford the education they will need to realize their dreams. To help them along, the Ashes are taking advantage of a new federal grant that supplements their contributions to a registered education savings plan, or RESP, by 20 per cent a year. It's motivating us to put more money aside," says Don, 39. "If someone wants to give you an automatic 20-per-cent return with no downside, I'll take it."

It's an offer many parents will find hard to refuse. And not only parents: Ottawa's Canada Education Savings Grant, introduced by Finance Minister Paul Martin in February's budget, is also open to grandparents and any other adult-whether related to the child or not-who wishes to contribute to a young person's education. The program, which is expected to cost taxpayers \$150 million in its first year-has its critics, and navigating the thicket of rules surrounding it can be a challenge. But the government's 20-per-cent sweetener, combined with growing concern over spiraling tuition fees, promises to make the once-unpopular RESP the hottest financial product since registered retirement savings plans-and a huge boon to the financial services industry. within three to four years," says Dan Richards of Marketing Solutions, a Toronto-based financial services consulting firm. "The majority of Canadians with young children will be taking advantage of this."

For years. RESPs were ignored by investors, hobbled by their low contribution limits and other restrictions. But a little cosmetic surgery in recent years has vastly increased the allure. RESPs have always allowed for a variety of investments, from mutual funds to guaranteed investment certificates. Since 1996, however, Ottawa has raised the annual contribution limit to \$4,000 from \$1,500, and last year it allowed RFSP funds to be rolled over into an RRSP if they are not used for a child's education.

Last February's grant announcement was the icing on the cake. Since then, some RESP providers report sales increases of as much as 50 per cent. And the number of RESP accounts, which stood at 750,000 in 1997, is expected to exceed more than 900,000 by the end of the year. The Big Six banks, which until recently only sold RESPs through their brokerage or trust operations, are moving quickly to sell RESPs directly. There's nothing more motivating for a family than seeing their child get the right education," says Bruce Armstrong, director of retirement services at the Bank of Nova Scotia, which hopes to sell RESPs from its branches this fall. "We recognize the power of that with Canadians, and we want to be a part of helping them achieve those goals."

The grant is not without its problems. The regulations surrounding it, which consume nine pages in the government's detailed budget documents, can be confusing. Along with regulations imposed by Revenue Canada and Human Resources Development Canada, the federal department that administers the grant, investors have to contend with the rules laid down by each firm that offers RESPs. They all have their own wrinkles, and each company differs ever so slightly from the other," says Monty Woodyard, manager of special projects at HRDC. "You really have to read the fine print."

The program also promises to be a bureaucratic nightmare for Ottawa. Multiple plans may be opened for one child as long as each contributor supplies the beneficiary's social insurance number and total contributions from all sources do not exceed \$4,000 a year. HRDC expects to process as many as 32

million RESP transactions a year. It will be up to the companies that sell RESPs-there are now about 40, and the number is rising quickly-to report any excess contributions. In addition, account holders who withdraw money after collecting the grant will have to repay the grant-provided that the company fulfills its obligation to report it. The terms of the government's agreements with RESP providers are still being negotiated. "We're really moving fast and hard in every direction to get everything together;" says Mary Elynn-McRae, a senior program officer for the Canada Education Savings Grant. "It's going to be quite a job, but it's not impossible."

Along with the confusion, the grant program faces opposition from some student groups. Instead of spending taxpayers' money on handouts that will primarily benefit middle-class families, the government should provide more funding to post-secondary institutions and push for lower tuition fees, says Brad Livigne, the 1997-1998 chairman of the Canadian Federation of Students. Failing that, the grants should go directly to students in need, he adds. The federation estimates that the cost of a four-year undergraduate arts degree, including living expenses, will rise from about \$40,000 today to \$67,000 by the time children born this year reach 18. The Bank of Montreal puts the future cost at about \$75,000, based in part on an assumption that tuition fees will continue to rise-as they have so far this decade-faster than the rate of inflation.

RESP promoters do not hesitate to trumpet those figures. But rather than taking the federation's advice, the government is attacking big-ticket tuition fees with the forces that move financial markets. Ottawa and the financial services industry are both hoping that fear, and a bit of greed, will ensure that Canadians save for their kids' increasingly high-priced educations.

## **How The Grants Work**

*The myriad rules surrounding registered education savings plans and Ottawa's new education grants could leave even seasoned investors scratching their heads. Some answers to common questions:*

### **How do parents sign up for the grant?**

Parents, grandparents or other adults wishing to contribute to the cost of a child's post-secondary education can take advantage of the grant by setting up an RESP through a mutual fund company, bank or other financial institution, which will apply for the grant on the customer's behalf. Several different types of RESPs are available, including individual plans that benefit one child, family plans and group plans that pool contributions from many investors. Self-directed plans for individual children or families may hold mutual funds, guaranteed investment certificates or other investments.

### **Can more than one adult contribute to a child's RESP?**

Yes, but total contributions may not exceed \$4,000 a year per child or \$42,000 over the life of the plan. Under Revenue Canada rules, contributions may continue for 22 years and the RESP must be dismantled after 26 years.

### **How is the 20-per-cent grant paid?**

Starting this fall, the money will be deposited directly into the RESP on a quarterly basis. The grant is paid on any amount up to the first \$2,000 contributed in a calendar year. The last instalment is paid in the calendar year the child turns 17. However, the grant will cease in the year the beneficiary turns 16 if the account contains less than \$4,000 or if contributors have failed to invest a minimum of \$300 a year in any four years. (Ottawa is considering lowering those requirements to \$1,500 or \$100 a year in any four years.) To receive the grant, the beneficiary must be a Canadian resident and have a social insurance number.

## **Can grant-contribution room be carried over from year to year?**

Yes. RESP holders whose contributions are too low to qualify for the full \$400 grant in a given year may carry over the remaining amount to the next year. But the maximum contribution in any year remains \$4,000, for a potential grant in the carry-over year of \$800. If a child is the beneficiary of several RESPs, the grant is paid on a first-come, first-served basis.

## **Are contributions tax-deductible?**

No, but earnings on RESP investments are sheltered from tax until the beneficiary enrolls in a postsecondary institution and begins collecting income from the plan. Most students will pay little or no tax on RESP money because they typically have little or no other income.

## **What if the child does not go to college or university?**

Parents who open individual or family plans may name another child as beneficiary, as long as he or she is a sibling by blood or adoption. If no sibling pursues postsecondary education, the face value of the grant-but not the interest-must be repaid to the government. Participants in some group plans also forfeit the interest on their money. Up to \$40,000 in an RESP may be rolled over into an RRSP over two years, provided the contribution room is available. That limit will be increased to \$50,000 next year. Money taken out of an RESP is taxed at 20 percent above the contributor's usual tax rate. However, the tax burden can be spread over two years and split between spouses.

## **What can RESP money be used for?**

RESP funds can be used for any education-related expense, including tuition, books, supplies and living expenses, provided the student is enrolled in a government-designated school in Canada or abroad.